

**Report of the
PUBLIC EMPLOYEE RETIREMENT
ADMINISTRATION COMMISSION
on the Examination of the
Somerville
Contributory Retirement System
For the Four Year Period
January 1, 1999 - December 31, 2002
PERAC 02: 09-083-32**

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January 6, 2004

The Public Employee Retirement Administration Commission has completed an examination of the **Somerville** Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, **1999** to December 31, **2002**. This audit was conducted in accordance with the accounting and management standards established by the Public Employee Retirement Administration Commission in regulation 840 CMR 25.00. Additionally, all supplementary regulations approved by PERAC and on file at PERAC are listed in this report.

In our opinion, the financial records and management functions are being performed in conformity with the standards established by the Public Employee Retirement Administration Commission with the exception of those noted in the findings presented in this report.

In closing, I acknowledge the work of examiner James Sweeney who conducted this examination and express appreciation to the board of retirement and staff for their courtesy and cooperation.

Sincerely,

Joseph E. Connarton
Executive Director

Somerville Retirement System

EXPLANATION OF FINDINGS AND RECOMMENDATIONS

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

1. Cash Reconciliation: The City Treasurer began reconciling the Retirement System's cash accounts in early 2003. The reconciliations reviewed by the auditor do not balance with the Board's General Ledger. The Treasurer is not supplying a list of outstanding checks to the Board and could not substantiate the reconciliations provided.

Recommendation: The City Treasurer shall be the custodian of the retirement system's funds according to G.L. c 32, § 23(2)(a). As custodian of the retirement fund, the Treasurer is obligated to perform a monthly reconciliation of all retirement system cash accounts. This process is necessary to maintain proper internal control of the retirement system by segregating reconciliatory duties. The Treasurer must forward appropriate paperwork (bank statement, reconciliation, and outstanding check list) to the retirement Board on a monthly basis. The retirement Board should then reconcile to the General Ledger and any checks outstanding for more than six months should be researched by the Board, so that the proper voiding and recording of these items can be completed. The Board must ensure that the Treasurer fulfill his/her obligation as custodian of the fund.

Board Response: The Somerville Retirement Board (SRB) has contacted the City Treasurer regarding this function that should be performed by the City Treasurer's office. A process has been implemented by which I am providing the Deputy Tax Collector (the person designated to perform the SRB's Cash Reconciliation) any and all documentation requested in order to properly complete this function.

2. Annual Statement: Based upon inspection of the Annual Statements filed by the Board for the four year audit period, it was determined that certain line item amounts contained in the Annual Statement did not match the detailed supporting schedules. Variances were found in realized and unrealized gains and losses.

Recommendation: As a sole source of information to third parties, the Annual Statement and supporting schedules must be in agreement allowing readers to make an accurate assessment of the systems financial condition without having to reference the general ledger. Prior to submission of the Annual Statement, a review process should be established to ensure all entries on the Annual Statement agree with the detailed supporting schedules using the PERAC Annual Statement Guide published each year. Differences in custodian-provided schedules should be corrected, if needed, and reconciled to the General Ledger prior to submission of the Annual Statement.

Board Response: Certain line items did not agree with attached detailed supporting schedules. I have implemented a process to track these items on a monthly basis to avoid this conflict in the future and informed auditor Jim Sweeney of PERAC who was physically present when I demonstrated this process. A larger issue exists here of reporting requirements between Pooled Fund managers and investment custodians. I have made Victoria Marcorelle of PERAC aware of these circumstances, as this is not unique to Somerville's Retirement System.

Somerville Retirement System

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

3. Appropriations: The Somerville Housing Authority pays their appropriation monthly. When it receives the bill for the next Fiscal Year, the Authority adjusts the monthly amount to coincide with their Fiscal Year (April to March). This results in both underpayments and overpayments during the July to June Fiscal Year.

Recommendation: Pursuant to G.L. c. 32, § 22(7)(iii) all units within the System must pay their total appropriation, as determined by the actuary, within the July to June Fiscal Year. The Somerville Housing Authority must pay the correct amount based on the same fiscal year as the Board.

Board Response: An issue exists regarding the appropriation being paid by the Somerville Housing Authority (SHA) to the SRB. It involves the timing of payments between SHA's fiscal year (March), the City of Somerville's fiscal year (June), and the retirement system's fiscal year (December). The SRB has been in communication with the SHA to correct this matter.

Final Determination

PERAC auditors will follow-up in six (6) months to ensure that appropriate actions have been taken regarding the audit findings.

Somerville Retirement System

STATEMENT OF LEDGER ASSETS AND LIABILITIES

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1999
AND ENDING DECEMBER 31, 2002**

FOR THE PERIOD ENDING DECEMBER 31,				
ASSETS	2002	2001	2000	1999
Cash	\$15,297,077	\$7,668,542	\$10,775,603	\$11,219,123
Short Term Investments	0	0	6,328,278	
Fixed Income Securities (at book value)	7,114,184	6,581,524	6,036,045	5,386,628
Equities	36,871,214	54,385,982	57,015,011	53,763,765
Pooled Short Term Funds	0	0	0	0
Pooled Domestic Equity Funds	0	2,969,384	0	0
Pooled International Equity Funds	4,403,670	4,885,958	6,426,869	7,243,434
Pooled Global Equity Funds	0	0	0	0
Pooled Domestic Fixed Income Funds	0	0	0	0
Pooled International Fixed Income Funds	0	0	0	0
Pooled Global Fixed Income Funds	19,539,116	17,944,594	16,745,497	15,193,567
Pooled Alternative Investment Funds	505,304	348,989	274,175	0
Pooled Real Estate Funds	11,957,013	10,189,165	8,407,276	10,069,343
Pooled Domestic Balanced Funds	20,967,745	18,802,236	17,958,348	17,294,401
Pooled International Balanced Funds	0	0	0	0
PRIT Cash Fund	0	0	0	0
PRIT Core Fund	0	0	0	0
Interest Due and Accrued	99,920	104,369	85,849	83,171
Accounts Receivable	4,938,942	4,541,436	4,325,499	5,620,952
Accounts Payable	0	0	0	(6,250)
TOTAL	<u>\$121,694,185</u>	<u>\$128,422,178</u>	<u>\$134,378,449</u>	<u>\$125,868,134</u>
FUND BALANCES				
Annuity Savings Fund	\$38,759,354	\$39,389,706	\$36,972,879	\$35,070,628
Annuity Reserve Fund	16,647,026	12,905,339	12,729,817	11,520,772
Pension Fund	2,308,288	3,094,922	2,918,867	3,520,324
Military Service Fund	7,211	7,111	6,979	6,835
Expense Fund	0	0	0	0
Pension Reserve Fund	63,972,306	73,025,100	81,749,907	75,749,575
TOTAL	<u>\$121,694,185</u>	<u>\$128,422,178</u>	<u>\$134,378,449</u>	<u>\$125,868,134</u>

Somerville Retirement System

STATEMENT OF CHANGES IN FUND BALANCES

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1999
AND ENDING DECEMBER 31, 2002**

	Annuity Savings Fund	Annuity Reserve Fund	Pension Fund	Military Service Fund	Expense Fund	Pension Reserve Fund	Total All Funds
Beginning Balance (1999)	\$32,523,989	\$11,238,393	\$5,060,396	\$6,688	\$0	\$67,257,935	\$116,087,401
Receipts	4,325,487	337,815	9,367,583	147	927,907	8,474,480	23,433,419
Interfund Transfers	(1,311,322)	1,298,113	(3,950)	0	0	17,159	0
Disbursements	(467,526)	(1,353,548)	(10,903,704)	0	(927,907)	0	(13,652,686)
Ending Balance (1999)	35,070,628	11,520,772	3,520,324	6,835	0	75,749,575	125,868,134
Receipts	4,910,500	403,212	9,349,740	144	1,107,037	7,809,503	23,580,136
Interfund Transfers	(2,275,368)	2,261,384	1,823,155	0	0	(1,809,171)	0
Disbursements	(732,882)	(1,455,551)	(11,774,352)	0	(1,107,037)	0	(15,069,821)
Ending Balance (2000)	36,972,879	12,729,817	2,918,867	6,979	0	81,749,907	134,378,449
Receipts	4,824,495	377,745	9,551,860	132	1,058,148	(5,934,985)	9,877,397
Interfund Transfers	(1,339,225)	1,339,218	2,789,831	0	0	(2,789,823)	0
Disbursements	(1,068,442)	(1,541,442)	(12,165,636)	0	(1,058,148)	0	(15,833,667)
Ending Balance (2001)	39,389,706	12,905,339	3,094,922	7,111	(0)	73,025,100	128,422,178
Receipts	5,065,421	337,815	10,166,574	100	989,537	(6,549,216)	10,010,231
Interfund Transfers	(5,125,136)	5,141,671	2,487,043	0	0	(2,503,578)	0
Disbursements	(570,637)	(1,737,798)	(13,440,251)	0	(989,537)	0	(16,738,224)
Ending Balance (2002)	<u>\$38,759,354</u>	<u>\$16,647,026</u>	<u>\$2,308,287</u>	<u>\$7,211</u>	<u>(\$0)</u>	<u>\$63,972,306</u>	<u>\$121,694,185</u>

Somerville Retirement System

STATEMENT OF INCOME

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1999
AND ENDING DECEMBER 31, 2002**

	FOR THE PERIOD ENDING DECEMBER 31,			
	2002	2001	2000	1999
Annuity Savings Fund:				
Members Deductions	\$4,222,117	\$3,865,389	\$3,762,330	\$3,463,727
Transfers from other Systems	202,480	222,778	398,979	108,805
Member Make Up Payments and Redeposits	130,318	55,316	47,072	59,553
Investment Income Credited to Member Accounts	<u>510,507</u>	<u>681,012</u>	<u>702,120</u>	<u>693,402</u>
Sub Total	<u>5,065,421</u>	<u>4,824,495</u>	<u>4,910,500</u>	<u>4,325,487</u>
Annuity Reserve Fund:				
Investment Income Credited Annuity Reserve Fund	<u>337,815</u>	<u>377,745</u>	<u>403,212</u>	<u>337,815</u>
Pension Fund:				
3 (8) (c) Reimbursements from Other Systems	31,606	71,968	100,148	48,950
Received from Commonwealth for COLA and Survivor Benefits	1,292,860	854,319	1,028,315	1,245,827
Pension Fund Appropriation	<u>8,842,107</u>	<u>8,625,573</u>	<u>8,221,277</u>	<u>8,072,805</u>
Sub Total	<u>10,166,574</u>	<u>9,551,860</u>	<u>9,349,740</u>	<u>9,367,583</u>
Military Service Fund:				
Contribution Received from Municipality on Account of Military Service	0	0	0	0
Investment Income Credited Military Service Fund	<u>100</u>	<u>132</u>	<u>144</u>	<u>147</u>
Sub Total	<u>100</u>	<u>132</u>	<u>144</u>	<u>147</u>
Expense Fund:				
Expense Fund Appropriation	0	0	0	0
Investment Income Credited to Expense Fund	<u>989,537</u>	<u>1,058,148</u>	<u>1,107,037</u>	<u>927,907</u>
Sub Total	<u>989,537</u>	<u>1,058,148</u>	<u>1,107,037</u>	<u>927,907</u>
Pension Reserve Fund:				
Federal Grant Reimbursement	150,767	137,030	134,031	147,211
Pension Reserve Appropriation	0	0	0	107,525
Interest Not Refunded	3,123	6,870	10,868	7,925
Excess Investment Income	<u>(6,703,106)</u>	<u>(6,078,884)</u>	<u>7,664,604</u>	<u>8,211,820</u>
Sub Total	<u>(6,549,216)</u>	<u>(5,934,985)</u>	<u>7,809,503</u>	<u>8,474,480</u>
TOTAL RECEIPTS	<u>\$10,010,231</u>	<u>\$9,877,397</u>	<u>\$23,580,136</u>	<u>\$23,433,419</u>

Somerville Retirement System

STATEMENT OF DISBURSEMENTS

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1999
AND ENDING DECEMBER 31, 2002**

FOR THE PERIOD ENDING DECEMBER 31,				
	2002	2001	2000	1999
Annuity Savings Fund:				
Refunds to Members	\$357,971	\$522,320	\$469,154	\$319,638
Transfers to other Systems	<u>212,667</u>	<u>546,122</u>	<u>263,728</u>	<u>147,888</u>
Sub Total	<u>570,637</u>	<u>1,068,442</u>	<u>732,882</u>	<u>467,526</u>
Annuity Reserve Fund:				
Annuities Paid	1,679,154	1,512,214	1,433,182	1,306,289
Option B Refunds	<u>58,644</u>	<u>29,228</u>	<u>22,369</u>	<u>47,259</u>
Sub Total	<u>1,737,798</u>	<u>1,541,442</u>	<u>1,455,551</u>	<u>1,353,548</u>
Pension Fund:				
Pensions Paid				
Regular Pension Payments	7,033,006	6,288,168	5,935,567	6,244,897
Survivorship Payments	422,269	279,909	286,560	413,208
Ordinary Disability Payments	124,925	126,367	167,586	208,637
Accidental Disability Payments	2,364,287	2,319,227	2,392,735	2,482,536
Accidental Death Payments	1,143,803	1,074,481	978,249	1,094,184
Section 101 Benefits	36,050	37,399	40,866	158,721
3 (8) (c) Reimbursements to Other Systems	330,339	327,818	302,823	301,521
State Reimbursable COLA's Paid	1,985,572	1,712,267	1,669,967	**
Chapter 389 Beneficiary Increase Paid	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>13,440,251</u>	<u>12,165,636</u>	<u>11,774,352</u>	<u>10,903,704</u>
Military Service Fund:				
Return to Municipality for Members Who				
Withdrew Their Funds	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Expense Fund:				
Board Member Stipend	13,750	15,000	14,867	15,000
Salaries	222,567	175,403	177,499	150,583
Legal Expenses	3,095	0	0	854
Medical Expenses	0	0	0	0
Travel Expenses	18,453	8,165	20,372	8,514
Administrative Expenses	58,550	53,338	59,702	37,355
Furniture and Equipment	0	6,975	230	2,997
Management Fees	628,822	755,420	789,063	712,977
Custodial Fees	44,300	43,847	45,303	(374)
Consultant Fees				
Sub Total	<u>989,537</u>	<u>1,058,148</u>	<u>1,107,037</u>	<u>927,907</u>
TOTAL DISBURSEMENTS	<u>\$16,738,224</u>	<u>\$15,833,667</u>	<u>\$15,069,821</u>	<u>\$13,652,686</u>

** Included in Regular Pension Payments

Somerville Retirement System

INVESTMENT INCOME

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1999
AND ENDING DECEMBER 31, 2002**

	FOR THE PERIOD ENDING DECEMBER 31,			
	2002	2001	2000	1999
Investment Income Received From:				
Cash	160029.19	438035.71	\$377,851	\$205,965
Short Term Investments	0	183,031	328,278	36,209
Fixed Income	451,759	425,483	367,492	245,271
Equities	674,612	646,225	627,378	543,205
Pooled or Mutual Funds	<u>3,420,655</u>	<u>3,729,087</u>	<u>3,716,012</u>	<u>3,840,320</u>
Commission Recapture	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
TOTAL INVESTMENT INCOME	<u>4,707,055</u>	<u>5,421,862</u>	<u>5,417,011</u>	<u>4,870,969</u>
Plus:				
Increase in Amortization of Fixed Income Securities	-	-	277,706	94,845
Realized Gains	1,797,607	2,477,268	10,579,310	3,987,547
Unrealized Gains	4,331,006	6,836,192	10,771,427	11,175,908
Interest Due and Accrued on Fixed Income Securities - Current Year	<u>99,920</u>	<u>104,369</u>	<u>85,849</u>	<u>83,171</u>
Sub Total	<u>6,228,533</u>	<u>9,417,829</u>	<u>21,714,292</u>	<u>15,341,471</u>
Less:				
Decrease in Amortization of Fixed Income Securities	-	-	(17,639)	(269,951)
Paid Accrued Interest on Fixed Income Securities	(27,968)	(40,078)	(27,489)	(45,302)
Realized Loss	(7,985,269)	(9,310,448)	(10,425,696)	(3,343,061)
Unrealized Loss	(7,683,130)	(9,365,163)	(6,700,193)	(6,179,804)
Custodial Fees Paid	-	-	-	-
Consultant Fees Paid	-	-	-	-
Management Fees Paid	-	-	-	-
Board Member Stipend	-	-	-	-
Interest Due and Accrued on Fixed Income Securities - Prior Year	<u>(104,369)</u>	<u>(85,849)</u>	<u>(83,171)</u>	<u>(203,233)</u>
Sub Total	<u>(15,800,735)</u>	<u>(18,801,537)</u>	<u>(17,254,187)</u>	<u>(10,041,351)</u>
NET INVESTMENT INCOME	<u>(4,865,147)</u>	<u>(3,961,846)</u>	<u>9,877,117</u>	<u>10,171,090</u>
Income Required:				
Annuity Savings Fund	510,507	681,012	702,120	693,402
Annuity Reserve Fund	337,815	377,745	403,212	337,815
Military Service Fund	100	132	144	147
Expense Fund	<u>989,537</u>	<u>1,058,148</u>	<u>1,107,037</u>	<u>927,907</u>
TOTAL INCOME REQUIRED	<u>1,837,959</u>	<u>2,117,038</u>	<u>2,212,512</u>	<u>1,959,270</u>
Net Investment Income	<u>(4,865,147)</u>	<u>(3,961,846)</u>	<u>9,877,117</u>	<u>10,171,090</u>
Less: Total Income Required	<u>1,837,959</u>	<u>2,117,038</u>	<u>2,212,512</u>	<u>1,959,270</u>
EXCESS INCOME TO THE PENSION RESERVE FUND	<u>(\$6,703,106)</u>	<u>(\$6,078,884)</u>	<u>\$7,664,604</u>	<u>\$8,211,820</u>

Somerville Retirement System

STATEMENT OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS	PERCENTAGE ALLOWED*
Cash	\$15,297,077	13.11%	100
Short Term		0.00%	100
Fixed Income	7,114,184	6.10%	35 - 80
Equities	36,871,214	31.61%	50
Pooled International Equity Funds	4,403,670	3.77%	5
Pooled Global Fixed Income Funds	19,539,116	16.75%	
Pooled Alternative Investment Funds	505,304	0.43%	
Pooled Real Estate Funds	11,957,013	10.25%	10
Pooled Domestic Balanced Funds	20,967,745	17.97%	
GRAND TOTALS	<u>\$116,655,323</u>	<u>100.00%</u>	

* The book value differs from the market value for individually owned Fixed Income Securities which are valued at amortized cost which is the original cost of the investment plus or minus any bond discount or bond premium calculated ratably to maturity. All other investments are reflected at their quoted market value.

For the year ending December 31, **2002**, the rate of return for the investments of the **Somerville** Retirement System was -3.85%. For the five year period ending December 31, **2002**, the rate of return for the investments of the **Somerville** Retirement System averaged 4.60%. For the 18-year period ending December 31, **2002**, since PERAC began evaluating the returns of the retirement systems, the rate of return of the investments of the **Somerville** Retirement System was 9.36%.

Somerville Retirement System

SUPPLEMENTARY INVESTMENT REGULATIONS

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

The **Somerville** Retirement System submitted the following supplementary investment regulations, which were approved by PERAC on:

February 19, 1992

18.02(4)

Rate of Return: A statement of the rate of return objective for the entire portfolio which shall be at least one percent (100 basis points) greater than a composite performance index consisting of thirty percent of the Standard and Poor's "500" Stock Index and seventy percent of the Salomon Brothers Broad Based Bond Index, cumulated quarterly.

October 29, 1992

16.02(4)

The board may employ a custodian bank and may charge such expenses against earned income from investments provided that such expenses shall not exceed in any one year .08% of the value of the fund.

June 30, 1994

20.03(1)

Equity investments shall not exceed 50% of the portfolio valued at market, including international equities which shall not exceed 5% of the portfolio valued at market.

20.04(1)

United States based corporations and equities of foreign corporations.

20.07(5)

Equity investments shall be made only in securities listed on a United States stock exchange, traded over the counter in the United States, or listed and traded on a foreign exchange.

September 21, 1995

20.03(2)

At least 40% but no more than 80% of the total portfolio valued at market shall consist of fixed income investments with a maturity of more than one year including Yankee Bonds and Eurobonds which shall be limited to 12% of the total fixed income portfolio valued at market.

20.04(6)

American Depository Receipts denominated in U.S. currency and listed on a United States stock exchange or traded over the counter in the United States, provided that the total of all such investments shall be considered part of the board's equity asset allocation and shall not exceed 10% of the total market value of the portfolio.

Somerville Retirement System

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

September 25, 1997

20.07(9)

Commingled real estate shall not exceed 10% of the total book value of the portfolio at the time of purchase provided that:

- (a) the retirement board does not participate in the selection of personnel responsible for making real estate investments and should this be required, prior to any participation by the board, the board shall consult with PERAC to determine the appropriate course of action;
- (b) such personnel retain authority in the decision making process, and
- (c) should an investment in real estate result in the direct ownership of real estate or mortgage indebtedness, such shall be permitted only until such time as divestiture is prudent.

December 18, 1997

20.03(2)

At least 35% but no more than 80% of the total portfolio valued at market shall consist of fixed income investments with a maturity of more than one year including Yankee Bonds and Eurobonds which shall be limited to 20% of the total fixed income portfolio valued at market.

January 9, 1998

20.06(2)

Bonds shall have a minimum quality rating of Baa or equivalent as rated by one or more recognized bond rating services, however, 4% of the market value of fixed income investments may be invested in bonds with a minimum quality rating below Baa or equivalent as rated by one or more recognized bond rating services.

20.06(4)

Fixed income holdings which are downgraded by one or more recognized rating services to below a Baa or equivalent rating must be sold within a reasonable period of time not to exceed one year, however, 4% of the market value of fixed income investments may be invested in bonds with a minimum quality rating below Baa or equivalent.

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

NOTE 1 - THE SYSTEM

The plan is a contributory defined benefit plan covering all **Somerville** Retirement System member unit employees deemed eligible by the retirement board, with the exception of school department employees who serve in a teaching capacity. The Teachers' Retirement Board administers the pensions of such school employees.

Instituted in 1937, the System is a member of the Massachusetts Contributory Retirement System and is governed by Chapter 32 of the Massachusetts General Laws. Membership in the plan is mandatory immediately upon the commencement of employment for all permanent, full-time employees.

The system provides for retirement allowance benefits up to a maximum of 80% of a member's highest three year average annual rate of regular compensation. Benefit payments are based upon a member's age, length of creditable service, level of compensation, and group classification.

Members become vested after ten years of creditable service. A superannuation retirement allowance may be received upon the completion of twenty years of service or upon reaching the age of 55 with ten years of service. Normal retirement for most employees occurs at age 65 (for certain hazardous duty and public safety positions, normal retirement is at age 55).

A retirement allowance consists of two parts: an annuity and a pension. A member's accumulated total deductions and a portion of the interest they generate constitute the annuity. The differential between the total retirement benefit and the annuity is the pension. The average retirement benefit is approximately 75 - 85% pension and 15 - 25% annuity.

Active members contribute either 5, 7, 8, or 9% of their gross regular compensation. Members joining the retirement system after January 1, 1979 must contribute an additional 2% on regular compensation earned at a rate in excess of \$30,000. The percentage rate is keyed to the date upon which an employee's membership commences. These deductions are deposited in the Annuity Savings Fund and earn interest at a rate determined by the Executive Director of PERAC according to statute. When a member's retirement becomes effective, his/her deductions and related interest are transferred to the Annuity Reserve Fund. Any cost-of-living adjustment granted between 1981 and 1997 and any increase in other benefits imposed by state law during that period are borne by the state.

The pension portion of any retirement benefit is paid from the Pension Fund of the System. The governmental unit employing the member must annually appropriate and contribute the amount of current year pension payments as indicated on the most recent funding schedule as approved by PERAC's Actuary. Until recently, retirement systems were paying only the actual retirement

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

benefits that were due each year. Systems had no statutory authorization to put aside any money for the future benefits of employees who are now working. Large unfunded liabilities resulted from operating upon this pay-as-you-go basis. In 1977, legislation authorized local governments to appropriate funds to meet future pension obligations.

In 1983, additional legislation was passed requiring the transfer of investment earnings (in excess of the amount credited to member accounts) into the Pension Reserve Fund. These initiatives have significantly reduced the rate of growth of the retirement systems' unfunded liabilities, and in some systems have actually eliminated such liability.

Administrative expenses are funded through investment income of the system.

Members who become permanently and totally disabled for further duty may be eligible to receive a disability retirement allowance. The amount of benefits to be received in such cases is dependent upon several factors including: whether or not the disability is work related, the member's age, years of creditable service, level of compensation, veteran's status, and group classification.

Employees who resign from service and who are not eligible to receive a retirement allowance or are under the age of 55 are entitled to request a refund of their accumulated total deductions. In addition, depending upon the number of years of creditable service, such employees are entitled to receive either zero (0%) percent, fifty (50%) percent, or one hundred (100%) percent of the regular interest which has accrued upon those deductions. Survivor benefits are extended to eligible beneficiaries of members whose death occurs prior to or following retirement.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Executive Director of Public Employee Retirement Administration Commission.

The Annuity Savings Fund is the fund in which members' contributions are deposited. Active members contribute either 5, 7, 8, or 9% of their gross regular compensation. Voluntary contributions, redeposits, and transfers to and from other systems, are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the Pension Reserve Fund. Upon retirement, members' contributions and interest are transferred to the Annuity Reserve Fund. Dormant account balances must be transferred to the Pension Reserve Fund after a period of ten years of inactivity.

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

The Annuity Reserve Fund is the fund to which a member's account is transferred upon retirement from the Annuity Savings Fund and Special Military Service Credit Fund. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually on the previous month's balance.

The Special Military Service Credit Fund contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.

The Expense Fund contains amounts transferred from investment income for the purposes of administering the retirement system.

The Pension Fund contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.

The Pension Reserve Fund contains amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the Pension Reserve Fund. Additionally, any investment income in excess of the amount required to credit interest to the Annuity Savings Fund, Annuity Reserve Fund, and Special Military Service Credit Fund is credited to this Reserve account.

The Investment Income Account is credited with all income derived from interest and dividends of invested funds. At year-end the interest credited to the Annuity Savings Fund, Annuity Reserve Fund, Expense Fund, and Special Military Service Credit Fund is distributed from this account and the remaining balance is transferred to the Pension Reserve Fund.

NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS

The **Somerville** Retirement System submitted the following supplementary membership regulations, which were approved by PERAC on:

December 26, 1984

- Regularly employed part-time employees working a minimum of twenty (20) hours per week must join the retirement system upon first date of employment.
- Provisional or temporary part-time employees working a minimum of twenty (20) hours per week must join the retirement system after working for six (6) consecutive months.
- No employees may join the retirement system unless they work a minimum of twenty (20) hours per week.

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

December 26, 1984

- All non-elected board members must join the retirement system upon the first date of employment.
- Election department employees paid by name for census are not eligible for membership in the retirement system.
- All new employees shall be examined by a physician and a written report shall be filed in the retirement system prior to their acceptance in the retirement system.
- Board members shall receive one (1) year of service for each year of service.
- Part-time employees who work at least twenty (20) hours per week shall receive one (1) year of service for each year of service.
- Seasonal part-time employees who work at least twenty (20) hours per week for seven (7) months or for the full season whichever is larger shall receive one (1) year of service of each year of service.
- The following formula shall be used for all hourly persons working for less than twenty (20) hours per week and for those seasonal employees who do not work for at least seven (7) months or the full season, whichever is longer:
 - number of hours worked per year - twenty (20)
 - the normal working period of the position
 - X 12 months = creditable service granted.

April 24, 1985

“To classify licensed electricians employed by the Somerville Housing Authority in Group 2 as of March 14, 1985”

March 28, 1988

Persons who were employed by the City of Somerville prior to January 1, 1984 and are being paid out of Federal Funds will become members of the Somerville Retirement System at an Annual Contribution Rate of 7%, due to the fact that they had been denied membership prior to that date.

August 19, 1993

All members of the Somerville Retirement System, whether they be full- time or part-time, shall be granted 12 months creditable service for each full year of membership.

November 29, 1994

To allow all full-time employees, including provisional and temporary, to join the Somerville

August 16, 1995

The “hazardous duty material” monies paid to Somerville Fire Department employees shall be considered as regular compensation.

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

May 19, 1998

- 1) That persons employed by the Election Department for working on the “census” may not pay a makeup for this time.
- 2) That draftsman (interns) hired by the Department of Public Works on a temporary basis will not join the Somerville Retirement System.

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

NOTE 4 - ADMINISTRATION OF THE SYSTEM

The System is administered by a five person Board of Retirement consisting of the City Auditor who shall be a member ex officio, a second member appointed by the governing authority, a third and fourth member who shall be elected by the members in or retired from the service of such system, and a fifth member appointed by the other four board members.

Ex officio Member: Edward F. Bean, Jr.

Appointed Member: Lawrence Murphy Term Expires: 4/1/2004

Elected Member: Mary A. Phinney Term Expires: 1/5/2005

Elected Member: John M. Memory Term Expires: 1/5/2004

Appointed Member: John E. Rourke Term Expires: 1/5/2003

The Board members are required to meet at least once a month. The Board must keep a record of all of its proceedings. The Board must annually submit to the appropriate authority an estimate of the expenses of administration and cost of operation of the system. The board must annually file a financial statement of condition for the system with the Executive Director of PERAC.

The investment of the system's funds is the responsibility of the Board. All retirement allowances must be approved by the Retirement Board and are then submitted to the PERAC Actuary for verification prior to payment. All expenses incurred by the System must be approved by at least two members of the Board.

The following retirement board members and employees are bonded by an authorized agent representing a company licensed to do business in Massachusetts as follows:

Treasurer - Custodian:)	
Ex officio Member:)	\$1,000,000 Each Employee and
Elected Member:)	Trustee, Employee Dishonesty
Appointed Member:)	Kemper insurance Company
Staff Employee:)	

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the System was prepared by **PriceWaterhouseCoopers** as of **January 1, 2001**.

The actuarial liability for active members was	\$101,419,719
The actuarial liability for retired members was	<u>103,137,804</u>
The total actuarial liability was	204,557,523
System assets as of that date were	<u>134,378,449</u>
The unfunded actuarial liability was	<u>\$70,179,074</u>
 The ratio of system's assets to total actuarial liability was	 65.7%
As of that date the total covered employee payroll was	\$44,779,084

The normal cost for employees on that date was 8.10% of payroll

The normal cost for the employer was 6.00% of payroll

The principal actuarial assumptions used in the valuation are as follows:

Investment Return: 8.30% per annum

Rate of Salary Increase: 5.75% per annum

GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2001

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a % of Cov. Payroll ((b-a)/c)
1/1/2001	\$134,378,449	\$204,557,523	\$70,179,074	65.7%	\$44,779,084	156.72%
1/1/1998	103,343,920	168,736,337	65,392,417	61.2%	38,969,295	167.80%
1/1/1995	67,754,043	127,119,756	59,365,713	53.3%	31,711,990	187.20%

Somerville Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2002

NOTE 6 - MEMBERSHIP EXHIBIT

Retirement in Past Years	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Superannuation	19	15	17	19	21	32	47	10	29	74
Ordinary Disability	2	0	0	0	0	1	1	0	0	1
Accidental Disability	6	5	6	4	1	1	5	0	1	6
Total Retirements	27	20	23	23	22	34	53	10	30	81
 Total Retirees, Beneficiaries and Survivors	 908	 898	 887	 881	 917	 902	 952	 896	 935	 976
 Total Active Members	 1,080	 1,130	 1,116	 1,134	 1,143	 1,182	 1,198	 1,232	 1,252	 1,185
 Pension Payments										
Superannuation	\$4,545,470	\$4,732,166	\$5,028,931	\$5,108,656	\$5,441,220	\$5,414,991	\$6,244,897	\$5,935,567	\$6,287,989	\$7,033,415
Survivor/Beneficiary Payments	174,119	163,169	160,771	275,747	275,999	286,194	413,208	286,560	279,909	422,269
Ordinary Disability	1,991,691	2,031,481	2,106,140	160,771	151,544	146,619	208,637	167,586	126,367	124,925
Accidental Disability	527,570	548,202	271,796	2,172,179	2,225,014	2,321,271	2,482,536	2,392,735	2,319,227	2,364,287
Other	<u>2,491,337</u>	<u>2,326,285</u>	<u>2,380,653</u>	<u>2,395,942</u>	<u>2,565,832</u>	<u>2,519,137</u>	<u>1,554,426</u>	<u>2,991,905</u>	<u>3,152,144</u>	<u>3,495,355</u>
Total Payments for Year	<u>\$9,730,187</u>	<u>\$9,801,303</u>	<u>\$9,948,291</u>	<u>\$10,113,295</u>	<u>\$10,659,609</u>	<u>\$10,688,212</u>	<u>\$10,903,704</u>	<u>\$11,774,352</u>	<u>\$12,165,636</u>	<u>\$13,440,251</u>